



**Remarks of
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It is always a special privilege to appear before the International Aviation Club, and I am grateful, therefore, for the invitation to speak to you today. If I had been able to predict more accurately the events that are unfolding this week, however, I might have suggested an alternative date – say, 2006.

I bring you greetings from my boss, Secretary Norm Mineta. I'm pleased to say the Secretary is back after a very successful surgery. His days as our first telecommuting Cabinet officer are coming to an end, and all of us at DOT are thrilled to have him back in the office.

A Time of Unprecedented Challenge

Let me just say at the outset that this is an extraordinarily sensitive time. This is not a crowd that needs any instruction from me regarding the current financial situation in the airline industry. We know that war with Iraq, whatever its duration, will exacerbate that picture. As I'm sure you know, the Administration is monitoring developments very closely. A group of airline CEOs met recently with the President's senior economic team, including four members of the President's Cabinet, to discuss the situation, and there have been countless other conversations at lower levels. We're also fully aware of the level of attention the industry is getting in Congress. It is being treated as a very serious issue.

One thing is clear: The airlines are focusing on costs like never before. They are embarked on a determined program of reducing the cost of providing air service in order to be able to provide that service at prices customers are willing to pay and still make a profit. Given the extent to which the cost structures of many of our major airlines now appear to be

fundamentally out of synch with what the market requires, this is an essential and probably long overdue undertaking.

And make no mistake: It is a painful process. Everyone in the industry is affected: Aircraft lessors and investors, aviation vendors, airports and their concessionaires, and – more than anyone else – airline employees.

Let me take a moment to say a special word about the men and women who staff our nation's airlines, who devote themselves every day to getting airline passengers where they want to go safely and efficiently. They are the essential ingredient in this great industry. It is they, when all is said and done, who will determine the future of their companies – not merely by the financial sacrifices that many will have made, but by the way they do their jobs.

Not many people noticed that we had zero fatalities in commercial aviation last year. A statistic like that doesn't come about by chance. Of course, our superb FAA air traffic controllers deserve an important share of the credit for that performance. But it's also eloquent testimony to the care and competence that airline employees bring to the job every day. At a time like this, with the industry challenged in so many ways, it also reflects a remarkable level of integrity. They deserve much greater recognition for their exemplary performance, particularly at a time like this.

It is important to recognize that there are some relatively brighter spots, even in this very cloudy landscape. For example, two very different types of carriers have emerged in our deregulated domestic airline industry – large network carriers on the one hand, and a newer group of low-fare airlines on the other. To a great extent they serve different types of markets, have different business strategies, and focus on different customers, even when they operate in the same geographic regions.

As you all know, network carriers traditionally have had much higher costs than their competitors in the other group. The cost structures of low-fare airlines have enabled them to provide capacity for price-sensitive passengers, a growing part of market demand, while also competing for time-sensitive business travelers based on their substantially lower prices.

There is another important difference between these two carrier categories – and it proceeds logically enough from the first difference: While the network carriers have been suffering losses and downsizing their operations, the lower cost carriers have continued to earn profits, expand operations, and gain market share.

Compared to their schedules in March 2001, for example, the low-cost carriers' share of available seat miles has increased by almost 50 percent – from 12.5 percent two years ago to over 18 percent today. The network carriers may well recapture some of this market share in the future, but it seems clear that low-cost, point-to-point carriers will represent a significantly larger share of the industry going forward.

So what does that mean? Should we conclude that the large, hub-and-spoke carriers are dinosaurs who have outlived their usefulness? Of course not. Low-cost carriers are an

increasingly important element in our commercial air travel system. But the traditional “major” airlines, through their feeder systems and code-sharing arrangements, serve an unmatched variety of markets – including a great many smaller communities that would not be on the aviation map without them. Over the course of many decades our largest airlines have established critical international franchises as well – links to foreign markets that are essential to trade and economic growth.

The simple truth is that this country needs the diversity of airlines that we enjoy in the market today, and the suggestion that we can do with just one category or the other is silly. That’s why we can’t be cavalier about any part of the industry, and why the Administration is watching developments so closely.

Aviation Reauthorization

Let me shift gears a bit and talk about infrastructure. One of the most dangerous things about a market as soft as the one we’re in at the moment is that it can create the illusion of adequate capacity. When resources are scarce, the temptation to take a respite from expansion can be hard to resist. But resist we must.

We are going to get through this. My personal conviction is that when we do, the industry will look a lot like the industry we have today, except that it will be more cost-effective, more competitive, and more robust. Maybe it’s hard to remember after all we’ve been through, but the summer of 2000 was characterized by the worst delay and congestion we had ever seen. If we don’t keep faith with our obligation to grow the system, there is no question that – sooner than you expect – we will again experience levels of congestion that call into question the ability of the industry to serve our economy.

Secretary Mineta is determined not to make that mistake. As many of you know, the Administration will very shortly unveil its proposals for the reauthorization of AIR-21, which expires at the end of this fiscal year. A lot of people at FAA and in the Office of the Secretary have spent a lot of time over the past several months developing those proposals, and we are proud of them. They will promote the industry’s growth and vitality while retaining safety as our top priority. We plan to reinforce our commitment to safety by making substantial investments in National Airspace System infrastructure and ensuring that our highly trained controller workforce is fully capable of sustaining its high levels of performance over the course of the next reauthorization period and beyond.

Our proposal will also ensure that we are prepared for the demand levels predicted in the FAA’s forecast earlier this week by continuing to fund airport capacity enhancements at record levels and modernizing the Airport Improvement Program. We will do all of this while continuing our quest to enhance competition at airports throughout the country.

I encourage you to stay tuned for more detailed news of the Administration’s reauthorization package. I think you will like it.

Looking to the Future

Let me offer a few comments on international developments, because they are so important a factor in the long-term vitality of the airline industry.

As many of you know, the European Commission is likely to get authority to conduct aviation negotiations with the United States sometime soon. If that happens, and the Commission is able to negotiate on behalf of all EU Member States, the likelihood is that it will propose a new and far more open structure for the trans-Atlantic air services market than we have today, even with so many Open Skies agreements linking the U.S. with EU countries.

The run-up to those negotiations has been clouded, I'm afraid, by some confusing developments, and some even more confusing rhetoric. First, a decision of the European Court of Justice last November found that some provisions of some of the Open Skies agreements between the U.S. and EU Member States were contrary to European law. The EU Commission immediately announced that the Court's decision meant that the Member States in question were obliged to "denounce" the offending agreements -- give notice to us that they intended to terminate them -- and to rely on the Commission to negotiate an EU-wide replacement agreement with the U.S.

The U.S., on the other hand, saw the ECJ decision as rather more surgical. The Court certainly held that a few provisions of the agreements were contrary to European law, but it didn't say that the agreements themselves had to be terminated. The U.S. promptly offered to amend the provisions in question -- none of which were central to the agreements in any event -- to conform them to European law.

We feel strongly that, whether these provisions are amended or not, it would be a mistake of the first magnitude to terminate the existing agreements. First, this is obviously the worst imaginable time to pull the legal and diplomatic rug out from under the trans-Atlantic air services market. There's plenty of instability and uncertainty in the market right now without any further complications from governments. The last thing airlines on either side of the Atlantic need is to be thrown into a state of uncertainty about the services they are allowed to provide.

Moreover, in many cases the Open Skies agreements the Commission was hoping to terminate are an absolute prerequisite to the ability of U.S. and European airlines to participate together in joint marketing alliances. Terminate the agreements and DOT's ability to approve them and confer antitrust immunity -- which depends on the certainty of an open market -- evaporates. Fortunately, the Member States appear to share these views, and so we are not anticipating any termination notices.

The problem with this episode is that it creates the false impression that the United States is somehow determined to preserve the status quo rather than negotiate with the European Commission. The truth is that we have looked forward for a long time to negotiating with the EU as a whole because it's likely that together we may find ingredients in a new arrangement

that enhance the ability of our airlines to expand their markets, serve them even more effectively, and even make money at it. What's important in the meantime is that we keep the door open to those negotiations and keep our minds open to new ideas.

I want to make it clear that, if and when those talks are launched, the government will proceed very deliberately, and in an open and accessible way. Many of you were around when we announced our Open Skies policy. That was a pretty radical departure at the time, but it didn't just spring from the government's head like Minerva; the policy was developed carefully, over a period of many months, in meetings with stakeholders throughout industry and government. By the time we found ourselves sitting across the negotiating table from a Dutch delegation in 1992, we knew where everyone stood, and we had a pretty good idea what the consequences would be for all stakeholders. And indeed, as controversial as it may have seemed at the time to open the vast U.S. market to KLM, the long-term economic benefits of the Open Skies policy have exceeded anything we could have imagined.

That's the model we envision for the conduct of U.S.-EU negotiations. And I can offer one further assurance: The outcome of those talks – if indeed they ever take place -- will be in the best interests of the United States.

Conclusion

And speaking of the United States, thousands of men and women in our Armed Forces are in harm's way today poised to rid the world of the scourge of Saddam Hussein at long last. Let's keep them in our prayers and hope that the hostilities end quickly and successfully. We want them home again soon.

Thank you for allowing me to share these thoughts with you today.

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